

MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY
OFFICE OF COMMUNITY DEVELOPMENT

**REFINANCING & CLOSING COST ASSISTANCE
IN HOMEOWNER REHABILITATION PROGRAMS**

Background: Many existing homeowners who apply for rehabilitation assistance have existing first mortgages with interest rates and terms that are not beneficial and in many cases unsustainable. Local programs have seen their liens extinguished by foreclosures when owners can no longer make their mortgage payments.

The Office of Community Development (OCD) has been asked whether grantees could use grant funds to pay closing costs associated with refinancing existing first mortgages as part of a homeowner rehabilitation project. This memo is intended to notify grantees that up to \$3,500 of closing cost and related assistance can be provided under certain circumstances, and to establish policies regarding acceptable terms and conditions for new first mortgages.

In addition to closing costs, other related costs, can be covered such as:

- Required homeownership counseling
- Funds to pay off open collections if required to obtain new first mortgage financing

Closing Cost Assistance as Eligible Homeowner Rehabilitation Cost

OCD grantees may provide up to \$3,500 in closing costs and related assistance to homeowner rehabilitation recipients to help them refinance unsustainable first mortgages. Specifically, assistance can be provided when the existing first mortgage:

- a. Has a balloon term of less than 10 years from the date of the application;
- b. Is an adjustable rate mortgage;
- c. Has an interest rate more than 2% above current market interest rates; or
- d. Results in a monthly payment such that the applicant's housing debt-to-income ratio is above 33% (and when refinancing to extend the term of the loan would bring payments below 33%).

To be clear, closing cost assistance to assist existing homeowners who are refinancing unsustainable first mortgages is **not eligible as a standalone activity**. Assistance can only be provided to applicants who are actually receiving rehabilitation assistance.

Required Counseling

MSHDA also expects that program participants receiving Closing Cost Assistance be provided with counseling from a MSHDA approved LINKS to Homeownership Counselor prior to closing on the refinancing transaction. Whether provided by grantee staff, the grantee's third-party administrator, or another local counseling agency, grantees may use part of the \$3,500 to pay for the counseling.

OPAL Implementation

A new line for Closing Cost Assistance is being added to Section A of the OPAL Homeowner Rehabilitation Proforma. Only the total of the closing costs and funds used to pay outstanding credit should with grant funds should be shown on this line. In the event a grantee assists an applicant with a refinancing transaction in which the homeowner's closing costs are financed as part of the new mortgage, no entry on this line is necessary.

Any closing cost assistance will be included within the Homeowner Rehabilitation Mortgage. The OPAL system will automatically calculate the minimum required mortgage amount.

Standards for New First Mortgage

In order to use grant funds to provide Closing Costs Assistance to an existing homeowner, the proposed new mortgage must meet the follow criteria which are based upon the standards OCD applies to its homebuyer programs:

- a. The interest rate should be no more than 100 basis points of the current national average 30-year fixed rate as published weekly by Freddie Mac (available online at <http://freddiemac.com>).
- b. Loans should be fully amortizing and have a minimum fixed-rate term of at least 30 years. MSHDA will not accept adjustable rate mortgages (ARMs), balloon loans, or interest only loans for first mortgage loans. In some cases, with prior permission from OCD, stepped interest rate loans may be considered that charge one interest rate for the first 24 or 36 months of the term and a slightly different interest rate for the duration.
- c. Closing costs must be competitive and reasonable. MSHDA will allow a 1% point origination fee and up to a maximum \$200 underwriting fee in addition to actual third-party closing costs (such as the appraisal, credit report fee, etc.). Additional fees paid to or collected by the lender or broker such as processing, commitment, and similar fees are generally not acceptable. Single-premium credit life insurance is not allowed under any circumstance as a required closing cost. The Office of Community Development does not allow the payment of points to buy down the interest rate.

Generally, closing costs allowed on MSHDA Single Family mortgages will be accepted on non-MSHDA mortgages. Attached is the current list of acceptable and unacceptable "Buyer Closing Costs and Other Fees" prepared by the MSHDA Single Family Mortgage office (also labeled as ***Attachment B to the Homebuyer Section of the Housing Resource Fund Summary***). If in doubt about the acceptability of any fees, please contact your CD Specialist for additional information.

- d. The monthly payment, including principle, interest, taxes, insurance, and mortgage insurance, should not exceed 33% of the household's gross income.

Additional Expectations

Grantees who propose to include Closing Cost Assistance intended to facilitate refinancing of participants' first mortgages must update their local program guidelines. Guidelines should cover the process by which grantees will identify applicants who may benefit from such assistance and the mechanics of providing that assistance.

Exceptions Require Prior Approval by OCD

Because many existing homeowners currently have both unsustainable mortgages and less than perfect credit, OCD expects that flexibility will be required in some cases. We expect situations in which an applicant may have less than perfect credit and only qualify for a sub prime mortgage with interest rates that exceed the standards but where the proposed refinancing is still in the client's best interest. If that applicant is, for example, in an adjustable rate mortgage paying 13.5% interest and can qualify for a fixed-rate mortgage at 9.0% that otherwise meets the standards above, an exception would likely be granted.

While there may be individual cases where these requirements may be waived, grantees should request specific exceptions in writing prior to making any commitments to prospective buyers who cannot qualify for loans meeting these criteria. Grantees are reminded that they will be responsible for representations and/or commitments made to applicants without prior approval.

File Documentation

Grantees should be sure that project files involving closing cost assistance include the following documents:

- a. A copy of the **signed loan application** to the new first mortgage lender, which should be substantially consistent with the homeowner's application for rehabilitation assistance.
- b. **Good Faith Estimate** (GFE) provided by the new mortgage lender. The GFE should be reviewed to ensure that the interest rate and closing costs are acceptable. Additionally, the estimated monthly payment (including estimates for property taxes and insurance in the event they are not escrowed as part of the new first mortgage) should be compared to the household's income projection to ensure that it is less than 33% of gross monthly income.
- c. **Settlement Statement** from closing of new mortgage.
- d. Copy of **check(s) disbursed** to pay off any open collections paid with OCD funds.
- e. Documentation of counseling session with **LINKS to Homeownership** approved counselor.

- f. Grantees requesting exceptions to any of the above should send a written request for an exception and should be prepared to provide OCD with copies of the above documentation and a copy of the homeowner(s)' credit report(s).

Refinancing without Closing Cost Assistance

It is a “best practice” for local programs to evaluate the quality and sustainability of any applicant’s existing first mortgage. In some cases, applicants may simultaneously benefit from refinancing their mortgage, be able to roll in their closing costs, and qualify to take cash out to pay for a portion of the rehabilitation project.

While OCD cannot require compliance with this policy in cases where local programs help families refinance without providing closing cost assistance, OCD strongly encourages that program participants still receive counseling and be required to take new mortgages that meet the standards outlined above.